97th Congress
2d Session

COMMITTEE PRINT

NATO AND THE ECONOMIC RECESSION

REPORT

OF

SENATOR DAN QUAYLE

TO THE

COMMITTEE ON ARMED SERVICES
UNITED STATES SENATE

AUGUST 20, 1982

Printed for the use of the Committee on Armed Services

U.S. GOVERNMENT PRINTING OFFICE

98-512 O WASHINGTON : 1982

5202-8

COMMITTEE ON ARMED SERVICES

JOHN TOWER, Texas, *Chairman*

STROM THURMOND, South Carolina	JOHN C. STENNIS, Mississippi
BARRY GOLDWATER, Arizona	HENRY M. JACKSON, Washington
JOHN W. WARNER, Virginia	HOWARD W. CANNON, Nevada
GORDON J. HUMPHREY, New Hampshire	HARRY F. BYRD, JR., Virginia
WILLIAM S. COHEN, Maine	SAM NUNN, Georgia
ROGER W. JEPSEN, Iowa	GARY HART, Colorado
DAN QUAYLE, Indiana	J. JAMES EXON, Nebraska
JEREMIAH DENTON, Alabama	CARL LEVIN, Michigan
NICHOLAS F. BRADY, New Jersey	

RHETT B. DAWSON, *Staff Director and Chief Counsel*
JAMES F. MCGOVERN, *General Counsel*
CHRISTINE C. DAUTH, *Chief Clerk*

LETTER OF TRANSMITTAL

U.S. SENATE,
COMMITTEE ON ARMED SERVICES,
Washington, D.C., August 20, 1982.

Hon. JOHN TOWER,
Chairman, Committee on Armed Services,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: During the period of July 6 to July 13 I was in Europe for the purposes of investigating several of the key economic, political and military issues which seem to be straining the NATO alliance, based on testimony recently given to the Armed Services Committee. Thirty-four meetings were held with U.S. officials and with foreign civilian and military leaders in Brussels, the Hague, Bonn, Paris, West and East Berlin, and London.

I would like to thank Don Imgram and Hank Steenstra of my staff who accompanied me on the trip and worked on the report. I would also like to express my appreciation to Peggy Burke for her work in preparing the report for printing.

The results of my findings are presented in this report and should be of interest and benefit to the members of our committee. As discussed, I believe that the alliance is facing the most serious crisis in its history, and considerable effort is required on the part of all member countries to prevent irreversible damage to our mutual defense interests and long-term political and economic relationships. I will subsequently present some recommendations in this regard to our committee as we consider matters relating to the NATO Alliance.

Sincerely,

DAN QUAYLE.

CONTENTS

	Page
Letter of Transmittal	III
Summary	VII
Background	1
Military Issues	2
NATO military status	2
Intermediate nuclear forces	2
Burden sharing	5
European Domestic Political Considerations	7
The peace movement	7
European political alignments	8
German reunification/East Germany	9
Economic Issues	10
The pipeline decision	10
The logic of the decision	11
The abruptness of the decision	14
Conclusions on the pipeline	15
Steel and agriculture	16
Conclusions	17

SUMMARY

The North Atlantic Treaty Organization is today facing the most serious crisis since its formation in the early post-war years. The world-wide economic recession, which most Europeans believe to be a consequence of high interest rates in the United States, seems to be at the root of many of the problems which are contributing to the crisis. Whatever the cause, depressed economies in Western Europe are causing NATO member countries to see the alliance in terms of their own parochial national economic interests, and defense related decisions—if not all of their decisions—are currently being made with a principal view toward their effect on local economies. In so doing, the countries seldom give due regard to the impact of their actions on the other allies.

Measures aimed at narrow economic self interest, including protectionist actions and liberal use of direct and indirect Government subsidies, are accordingly being implemented with increasing frequency. The European attitudes and actions on the pipeline, steel dumping, and agricultural exports are examples.

Such actions combined with constraints on, and in some cases reductions in, defense spending, may inevitably lead to reductions in NATO force levels by some countries. These could further raise friction levels within the alliance as member countries question and complain about the contributions of others. Such feelings could precipitate retaliatory actions against military spending in general.

Out-of-power political parties can be expected to use the current economic situation to advantage, offering sharp criticism of defense spending plans and specific weapon system acquisition plans. They also likely will pick up on the defense debates in other NATO countries, and if one nation reduces its spending and/or its force levels, they will agitate for similar reductions in their own countries.

While the peace movements are relatively quiet at the present time, I can foresee them causing real problems in completing NATO plans for modernization of theater/tactical nuclear forces. Certainly the Soviet Union, which has financially and organizationally abetted previous European demonstrations, can be expected to resume its campaign against the Pershing II and Ground Launched Cruise Missile programs. Despite reassurances and rhetoric to the contrary, I am concerned about whether or not the program to place the missiles in Europe will move forward on schedule.

The "two-track approach" to negotiations for Intermediate Nuclear Forces is discussed in different terms in Europe than intended by the United States. Our initial intention was to negotiate with the Soviet Union while simultaneously implementing arms modernization plans. In this manner, the Soviet Union would be under continuing pressure to reach a mutually equitable arrangement at the earliest possible moment. Many of our NATO allies, however, see the two tracks as

BEST AVAILABLE COPY

alternatives, rather than simultaneous events. They see theater nuclear modernization being required if negotiations fail, but are hesitant to be unequivocal about proceeding with actually putting missiles in place while negotiations are in progress. We therefore can expect that the Soviets will try to stall the negotiations, while bringing pressure on NATO countries to place a freeze on reequipment plans while talks are in progress. West Germany, whose constitutional policy is to take no action which will worsen the prospects for eventual reunification, is particularly subject to such pressure, despite West German protests to the contrary.

The basic U.S. attitude and policy toward trade with the Soviet Union is openly questioned throughout NATO. Any talk of waging "economic warfare" with the Soviets terrifies most Europeans. They also see a lack of consistency in our actions, and question our ability to lead the alliance. The recent pipeline decision is denounced in very vehement terms in NATO. They scornfully point to our continued grain trading as an example of a lack of a definitive and consistent policy.

Altogether, I believe the seeds are being sown for a serious political weakening of NATO which may in turn lead to a weakening in military capability and resolve. With elections in the offing in several NATO countries, further deterioration seems possible.

When one reflects on the potential causes of armed conflict which could lead to the demise of Western civilization, the concern usually focuses on relative military strength and the credibility of deterrence. Though providing a viable deterrence to the Soviet threat is a challenge which cannot go unmet, the potential for a disaster may well arise more from economic failure than from military weakness or imbalance.

In this day of abstract potential of nuclear holocaust, it is easy to emphasize our military concerns for survival rather than our economic concerns, but we cannot avoid the fact that current world-wide economic problems can escalate into military actions. It is worth remembering that World War II was triggered as much by the economic isolation of the Axis powers as by irrational or power-thirsty dictatorships.

With so many divisive factors at work tending to split the alliance, it will take a major United States and overall NATO effort to prevent the current economic problems from causing long-term damage to our relationships. For the United States, the required actions may be difficult to implement in light of the growing feeling amongst the U.S. public and some members of Congress that we are over committed to, and over spending on, NATO. This feeling is compounded by the growing isolationist pressures in America.

Partisan political speeches that may be made in the United States this fall, while principally intended for domestic consumption, may exacerbate the economic and military situation and further strain NATO relationships. An example is the call for a nuclear freeze in the United States at a time when it is touch-and-go in Europe as to whether the nuclear modernization plans can be implemented. Speeches in the United States calling for a freeze on nuclear weapons programs, including cruise missiles, will weaken the ability of NATO politicians to proceed with their own programs.

As a final observation, and perhaps the only positive one emerging from my meetings in NATO, the Soviet Union and its Warsaw Pact allies are undergoing similar economic, political and military upheavals, also brought on by economic difficulties and the enormous cost of their sustaining a near war-time economy. As stated during one of my meetings, the Soviets have a near unsolvable problem in Poland which is being carefully watched by other Warsaw Pact countries. The Soviets must also pause to think about the experience of the Falkland Islands which showed that a NATO country, with the emotional and tangible support of other NATO countries, had the political will to use force of arms in defense of its interests. They must also consider the results of the Israeli attacks on Syrian aircraft and missiles in Lebanon, where Soviet hardware has been proven wanting in the face of modern Western/U.S. technology. The implications of this on the balance of conventional military power in Central Europe will be the subject of much analysis and speculation on the part of both NATO and the Warsaw Pact.

The details of my findings are contained on the following pages.

NATO AND THE ECONOMIC RECESSION

BACKGROUND

The Senate Armed Services Committee has been extensively briefed on NATO defense spending and related issues over the past six months. Many positive words were expressed in formal testimony by Defense Department and other Administration officials on behalf of our allies. Nevertheless, many Senators were left with the disquieting feeling that all was not well within the alliance. There seemed to be a lack of agreement on the seriousness of the Soviet threat, and on the defense contributions required of each member country. Very serious questions arose in the minds of some members as to whether or not NATO was doing its fair share.

Such questioning of our allies has also become a very serious domestic political issue with our constituents, many of whom express the opinion that, literally, "if the European NATO countries are unwilling to spend enough to provide for their own defense, why should the United States assume the burden of defending a disinterested NATO?" While such views do not take into account the fact that defense of Western Europe is absolutely essential for U.S. security, the public nevertheless is clamoring for some modification of our policies in Europe. Probably stimulated by concerns of the recession and high unemployment, some have even suggested that we reduce (or eliminate) the complement of U.S. forces now stationed in Europe. Similar suggestions have been offered by several Members of Congress, some from the viewpoint of taking punitive actions against recalcitrant allies, and some from the pragmatic viewpoint of simply reducing defense spending in the area (NATO) which accounts for over half of all U.S. defense spending.

A basic question arose in my mind, therefore, as to what were our expectations about the contributions of our NATO allies, what were their commitments, and were they living up to them? It was with that consideration in mind that I co-sponsored, with Senator Levin, an amendment to the fiscal year 1983 Defense Appropriations Authorization bill which required the administration to report to Congress on NATO spending.

My visit to Europe during the July 4 recess was a logical next step in pursuing these concerns. I also used these discussions to form impressions on the individual views of NATO countries on strategic disarmament talks, their positions on Intermediate Nuclear Force negotiations, the effects of peace movements, and their respective attitudes on economic and trade issues.

The meetings began on July 6, 1982, and were completed on July 13. The places visited included: Brussels, Belgium; NATO Headquarters (Brussels); The Hague, The Netherlands; Bonn, West Germany;

BEST AVAILABLE COPY

Paris, France; West Berlin and East Berlin; and London, United Kingdom.

Thirty-four meetings were held with U.S. and foreign personnel, including U.S. ambassadorial level and country-team individuals. The foreign officials included parliamentarians of both incumbent and out-of-power parties, defense and foreign ministry officials, military people, and non-government defense analysts. Discussions were also held with individuals concerned with economic issues and with U.S. trade relations.

Based on these discussions, I received strong impressions on several of the key issues facing the alliance, as seen by our allies. These are individually discussed below.

MILITARY ISSUES

NATO MILITARY STATUS

In general, I was relatively pleased with the current military situation in Central Europe. Although serious deficiencies still exist in our conventional capability, the results of recent spending to improve readiness are evident. However, in light of the more pressing economic issues which dominated discussions during this visit, admittedly only a small amount of time was spent on issues of purely military status and readiness. Each NATO country seemed to have a good comprehension of the military role it was expected to play in the NATO alliance, and seemed to be reasonably well manned and equipped to fulfill that obligation.

Military leaders uniformly expressed pride in the capability and motivation of their forces and seemed prepared to implement NATO plans. They were especially proud of the quality of the individuals in their armed services, which they indicated were probably superior to the quality of U.S. Army personnel in Europe. The NATO people attributed this difference to their use of conscription while the United States relies on an all-volunteer force.

A number of Europeans questioned our lack of a draft, usually in response to our questioning their NATO contributions. Literally, if they can sell a draft to their people, why can't we sell a draft to the U.S. public?

While there is good agreement on NATO's current strategy for fighting a war in Central Europe, there is less certainty about the future, and the feelings developing in the United States that the current strategy requires significant revisions. Few people talked about the newer concepts being proposed and evolved that would greatly enhance the alliance's ability to wage conventional war (for example, the "Air-land Battle" thinking). Action is required to bring European NATO members up to speed in this area, and to develop an agreed-upon strategy for the future. The prospect of improved conventional capability without greatly increased growth in defense spending is encouraging and warrants serious attention. Senator Sam Nunn's report to the Senate Armed Services Committee, "NATO: Can The Alliance Be Saved?", May 13, 1982, deals with this issue and deserves considerable attention.

INTERMEDIATE NUCLEAR FORCES

The only common viewpoint expressed by all our allies seems to be the strong conviction that NATO must continue to have an unequivocal policy that it is prepared to respond to a Soviet conventional attack with nuclear weapons. Our allies believe it is sheer insanity to subscribe to a no-first-use policy, because NATO will never commit enough resources to equip itself with sufficient forces and equipment to fight and win a conventional war. They believe we must retain the option for first use, and at least leave the nuclear factor uncertain enough in Soviet planners' minds that they would be deterred from a conventional attack on us.

This theater nuclear policy is, of course, a deterrent policy, intended to dissuade the Soviets from initiating a conventional war. It is also intended to prevent the Soviets from amassing overwhelming forces in a given geographical area, sufficient to achieve a rapid breakthrough. By forcing the Soviets to spread their forces to minimize the effectiveness of potential allied nuclear retaliatory attacks, NATO can maximize the effectiveness of its conventional forces.

The Soviet deployment of intermediate nuclear weapons—well over 300 SS–20's to date—has posed a threat to Western Europe unrivaled in the post-World War II era. The balance of power in theater nuclear weapons has shifted from a NATO advantage to one of great Soviet tactical superiority, absent modernization of NATO theater nuclear weapons. It was precisely because of this imbalance that NATO agreed in 1979, at the urging of West Germany and contrary to the position of the United States, to deploy Pershing II and ground launched cruise missiles. This was the "two-track" decision, to proceed with deployment of these missiles while the United States sought to obtain agreement from the Soviet Union to dismantle their SS–20 force.

Although the original decision was that these two tracks were to proceed simultaneously, the current, near universal European interpretation of the meaning of "two-track" is that while site preparation will be ongoing, actual missile deployment will begin only if INF negotiations fail to produce agreement.

As one discusses INF deployment in Europe today, it takes some effort to keep in mind that the subject of modernizing NATO's nuclear capability with ground based missiles began as a European idea. However, it was a specific proposal of Chancellor Schmidt that formed the basis for the 1979 "two-track" decision to deploy ground launched cruise missiles and Pershing II's. When the United States objected to this concept and urged submarine launched cruise missiles as an alternative, West Germany and others in Europe insisted that visible, land-based missiles were a vital part of the European deterrent. When one now hears the United States making arguments for the 1979 decision and trying to prop up the resolve of at least some of our allies, the impression is created that modernization of land-based missiles is an idea the United States is forcing on them. The fact is that it was a European, and specifically German, request that led to current INF planning.

Of the countries visited, only Great Britain seems to be unqualified in its commitment to deploy the new missiles, although I am assured that Italy remains similarly firm. Although both the Belgian and Dutch governments remain officially committed to deployment, it seems to be the general consensus in Europe that while the Belgians

may proceed to actual deployment, it is very unlikely that The Netherlands will see their program through to completion.

Although no site selection announcement had been made by the Belgian Government at the time of my visit, it was a matter of some interest that one of the candidate site selection locations, the city of Florennes, had conducted a straw poll in which some 80 percent of those voting had opposed deployment of missiles. Belgian officials were quick to point out that only 42 percent of eligible voters had participated, and further asserted that in a hypothetical official election with the usual Belgian requirement of mandatory voting, the 58 percent who didn't vote would support deployment. Whatever the merits of their assessment of that straw poll, the Belgians spoke in very positive terms about their resolve to go ahead with site selection and preparation and, if the talks fail, with cruise missile deployment.

Germany clearly presents the largest and most important question mark. Although the official commitment of the government, the personal prestige of Chancellor Schmidt, and the support of the opposition Christian Democratic Union are behind deployment, questions still remain. The Germans have recently imposed qualifications on their deployment commitment as they have seen wavering in other countries and have felt internal pressures from the peace movement.

It is clear that the Germans would like to have the other three continental countries (Italy, Belgium, and The Netherlands) deploy as they agreed to in 1979. They have made it a requirement that there be at least one and possibly two other continental countries (in addition to Great Britain) that go through with deployment. It has also been suggested by the Germans that emplacement of the missiles in the various countries be esssentially simultaneous. More disturbing yet are recent reports that the newly proposed German defense budget will not include funds needed for missile site preparation. This could have a serious negative effect on the INF negotiations. For reasons which are discussed below with respect to the peace movement and fragile political alignments in some European countries, there are several factors at work which put into question whether the resolve to proceed with deployment will hold firm. Thus, even as one hears brave sounding words from various German politicians about their determination to deploy, and about not sending the wrong signals to the Soviets about Western resolve, one must ask whether the Germans will proceed with deployment on schedule in December 1983, if the INF talks fail.

Complicating these questions about the positions of our allies is concern about Soviet strategy in the INF talks. Will they attempt to exploit the wavering European resolve by making a proposal which they know the United States will not accept, but which sounds sufficiently intriguing to certain European ears that they will defer deployment because the talks (in their view) have not failed? Will the Soviets attempt to drive a wedge in the alliance by making an offer which includes taking some account of British or French weapons? These are the kinds of questions being asked in Europe today, the disturbing part being the fact that at least the French and British are uncertain of what the response will be elsewhere in Europe.

Discussions with both the French and British made it absolutely clear that they are irrevocably opposed to any concession by U.S. negotiators in the INF talks which counts French or British missiles in any nuclear balance calculations. Both countries view their nuclear capability as their strategic deterrent force. As such, their missiles have no place in a comparison of theater nuclear forces of the Soviets and NATO. Both Britain and France are concerned that this issue will be one which the Soviets will seek to exploit in the hopes that it will be sufficiently attractive to West Germany to cause them to delay putting the new missiles in place.

Any discussion of deployment of INF missiles must take note of another message which came across loud and clear in my meetings, particularly from the military people we talked to. It is that the Soviets have a very great fear of the deployment in Western Europe of Pershing II and ground launched cruise missiles which have a range which includes Soviet territory. Thus, the Soviet incentive to negotiate seriously in Geneva seems very great. The same people who made this point also made the point that the Soviets will not negotiate for the removal of SS–20 missiles unless they are convinced that NATO will actually deploy its missiles, and that the only way to avoid that deployment is to remove the SS–20's. Some people in Europe are very concerned that the U.S. ability to negotiate from strength in Geneva will be undermined if the Soviets are not convinced that deployment will occur. Hans-Dietrich Genscher, Minister for Foreign Affairs of the FRG, made these comments on January 29, 1982, in Davos, Switzerland:

> The aim of the Alliance is a zero-level outcome, in other words, a solution in which the Alliance completely forgoes modernization with medium-range missiles, if the Soviet union for its part completely scraps its medium-range missiles.
>
> However, the negotiations in Geneva between the United States and the Soviet Union will only lead to success if the Soviet Union is not left in any doubt that the Western medium-range missiles will be deployed if a disarmament agreement is not reached by the end of 1983. In other words, anyone in the West who advocates the renunciation of Western modernization or calls for a moratorium is arousing Soviet illusions and undermining the Geneva negotiations.

Based on similar views expressed to me during this trip, there is good reason for that concern.

BURDEN SHARING

When I raised the issue of whether or not NATO will meet the 3 percent commitment, most of our NATO allies responded that they have more than held their own on spending over the last decade, and that it is the United States alone that has been remiss in defense spending. For the record, the following is a chart showing a comparison of defense spending of NATO countries for 1979, 1980 and 1981:

NATO COUNTRY DEFENSE SPENDING IN TERMS OF PERCENT CHANGE IN REAL DEFENSE SPENDING

[Percent change from previous year in constant prices excluding inflation]

	1979 or 1979–80	1980 or 1980–81	1981 or 1981–82	1982
Belgium	2.2	2.0	0.2	
Canada	−.9	5.1	3.0	
Denmark	.2	.7	.1	
France	2.5	3.9	3.5	
Germany	1.8	1.9	1.9–3.4	
Greece	−2.9	−8.8	5.6	
Italy	2.6	4.9	−1.2	
Luxembourg	3.5	16.3	7.1	
Netherlands	3.9	−1.5	2.3–3.4	
Norway	1.9	1.8	2.5	
Portugal	2.9	10.1	2.8	
Turkey	2.6	2.0	3.1	
United Kingdom	3.0	2.7	2.1	
Comparison with U.S. spending:				
United States	3.4	4.9	5.4	
Non-United States-NATO	2.7	2.6	2.2–2.6	1.6–2.1

Source: Data from Secretary of Defense Weinberger's March 1982 report to Congress.

Despite enormous current pressure from the United States for them to increase their spending plans beyond the agreed-upon 3 percent target figure, few countries, if any, seem ready to increase their planned expenditures. With the generally poor economic health of most European economies, and with impending elections in several countries, it is probably unrealistic to believe that additional pressure will produce anything more than token readjustments to their defense spending. Rather, reductions below published figures seem much more likely. Should these occur in one country, other countries may find it politically impossible to maintain their own levels, and a kind of domino effect might occur.

I am particularly concerned about force levels amongst the NATO members, and the interplay of one country's actions on others. Abrupt U.S. force reductions as a punitive measure would probably be counterproductive and only result in counter-moves by our allies, with further escalation of tensions. Reductions in U.S. force levels pragmatically forced upon us because of limits on our own spending plans will also probably make it politically expedient for our allies to follow suit, as out-of-power European parties demand similar cutbacks. The converse will probably also prove true, and if European countries reduce their force levels due to their own internal problems, there will be many demands in the United States for withdrawal of part or all of the U.S. forces.

Of particular concern this year is the West German defense budget. The proposed defense budget will show, at best, no real growth—just keeping up with inflation. If inflation turns out to be worse than predicted, the balance sheet may well show a loss in defense growth. In either case, there is a good possibility that troop reductions as large as 20,000 individuals may occur, along with a smaller commitment for funding of host nation support and INF missile site preparation.

BEST AVAILABLE COPY

Whatever its real impact on NATO defense capabilities, if a West German troop reduction were to be announced in the context of no real growth in defense spending, calls to "bring the troops home" can be expected to be heard in the United States again, and with greater fervor. In this scenario, there is also the likelihood of no funding for the forward basing of the U.S. Army (much nearer to the inter-German border) reflecting what appears to be a strong German reluctance to support this idea. In previous comments on the INF deployment, I indicated how serious a lack of such funding for missile site preparation would be for the INF negotiations. While the Germans may have good reason to point with pride at their steady growth in defense spending over the last decade, a no-growth budget will be viewed with alarm in many quarters.

Despite the economic problems in France and Great Britain, defense officials in both countries expressed optimism that they will have real growth in their 1983 defense budgets. The French expect to have real growth of about 2 percent and the British hope to be close to 3 percent, not including the costs of the war in the Falkland Islands. If these forecasts hold true, it is encouraging news. While they are not likely to meet the goal of 3 percent real growth, both Belgium and The Netherlands also expect to show some real growth in 1983.

DOMESTIC POLITICAL CONSIDERATIONS

THE PEACE MOVEMENT

Despite the ominous and anti-American appearance which the European peace movement has had in the United States, one gets a different perspective from Europeans. They see the peace movements—primarily in The Netherlands, West Germany, and Great Britain—as consisting of a small core of radicals with communist support, but swelled by a much larger number of people disturbed by talk of a winnable nuclear war, by INF deployment plans, by nuclear power plants, and even by Soviet SS–20s. What a number of people took pains to point out to me is that President Reagan's zero-option INF proposal was well received by the more responsible elements in the peace movement, and has largely defused the desire for public demonstrations—at least for the time being. At the same time, Europeans mentioned the very large peace demonstration in New York City which seemed to take no account of the President's proposals on either INF or START. In addition, they express amazement and shock at what they view as incredibly naive calls by U.S. people for a nuclear freeze. They also made the point that when an American political party adopts a nuclear freeze as part of its platform it not only tends to weaken the United States position on any negotiations but also tends to encourage European anti-nuclear politicians and protesters alike. It is perhaps with some real justification that they view the peace movement in the United States with greater alarm than the movement in Europe.

While acknowledging the present lull in Europe, leaders in all the countries are concerned about the potential for a very vigorous, and perhaps more violent resurgence of the peace movement should the

INF talks fail (or stall) and the NATO countries begin actual deployment of the Pershing and cruise missiles. One must wonder, along with many of the European politicians with whom I met, whether the political leaders at the time will have the political courage and the public support to proceed to actual deployment in the face of demonstrations or the threat of violence. In this context they express real concern about the potential impact of pro-freeze, anti-nuclear statements, to be made during the U.S. political campaigns this fall, on the INF negotiations. These same politicians also express concern about how the Soviets might seek to exploit the fact that demonstrations loom in the background by offering up a proposal sufficiently attractive to convince demonstrators of its merit, but so insubstantial that our negotiators will consider the talks to have failed. For many Europeans this is the most worrisome INF scenario.

EUROPEAN POLITICAL ALIGNMENTS

Discussions in the countries I visited, including those with parliamentarians of all parties, indicated that the expectation is that the next elections in most countries will show a definite conservative trend. Mrs. Thatcher and her Conservative Party are expected to strengthen their parliamentary majority. While the British success in the Falklands makes that a near certainty if elections are held soon, most observers think that will be the case even after the post-Falklands euphoria has worn off.

In Germany, the CDU/CSU is widely predicted as being able to defeat Chancellor Schmidt's Social Democratic Party. While it is believed this could happen at any time, a number of people suggested that the Christian Democrats would prefer to wait and not take power at a time of general economic difficulty.

The consensus in The Netherlands is that this fall's elections will likely see a government formed from a more conservative coalition of the Christian Democratic and Liberal (conservative) parties.

Although the French government is controlled by the Socialists and includes Communists in the cabinet, the Mitterand government is expected to continue its already established record of the same strongly pro-defense attitude of past French governments.

Despite these trends, it is by no means certain that the voters will elect conservative governments sufficiently strong to withstand the anti-nuclear fervor of the peace movement. Contributing to this concern is the rising political strength of radical new parties such as the Green Party in Germany. These parties are typically composed of people with environmental and anti-nuclear (nuclear weapons and nuclear energy) concerns. As "one-issue" parties they will not likely become part of coalition governments. Thus, while they tend to be only a negative factor, if they can get 7 to 10 percent of the vote and achieve parliamentary representation (as seems likely in Germany), they may make formation of a workable coalition very difficult. Throughout the trip I heard concerns expressed about this growing phenomenon in a number of European countries.

Another concern expressed by many Europeans is the expectation that the out-of-power political parties, particularly on the more

radical left, will use the current economic problems of high unemployment and increasing inflation to political advantage, and will be especially critical of the share of the budgets going to defense spending. The Conservatives in Great Britain have already felt this pressure and it is expected to increase in Germany should the CDU/CSU take power. Some people in Germany suggested that the CDU/CSU may find it far more difficult to maintain solid support for budgets that include defense growth than has the Schmidt government, which has held the conservative element of the Social Democrats together while getting strong support from the opposition CDU/CSU.

GERMAN REUNIFICATION/EAST GERMANY

I was surprised at how deep-seated is the viewpoint of West Germans that any action they take must not be a step backward in the path toward eventual reunification, which is a goal specified in the West German constitution. Whereas most U.S. citizens tend to have adopted the pragmatic approach that reunification of Germany will not occur other than in the context of a general upheaval in the Soviet Union and its satellites which deposes their communist governments, many West Germans consciously consider reunification issues in all their decisionmaking. Thus, they consider whether the impact of completing the installation of Pershing and cruise missiles will be detrimental to reunification efforts. Such an attitude can easily be exploited by the East Germans and Soviets, who can exercise pressure by the simple expedient of playing to the yearnings of divided German families. Control of access to and from East Germany is key in this regard.

While prohibiting its general populace from leaving East Germany for the West, the East German government permits pensioners over age 65 to leave. West German policy allows for these pensioned East Germans to resettle in West Germany and to receive their pension and medical benefits from West Germany. While freeing the East German Government from such costs and while callously "getting rid of" the elderly, the practice accentuates the fact that Germany is a divided nation with split families, most of whom remain in contact with one another.

Access by West Germans to East Germany is permitted, but requires that each West German visitor exchange 25 DM (now approximately $10) for an equal number of East German marks at the border. Since this one-for-one exchange rate falls far short of the bank rate of exchange (of up to eight to one in favor of West German marks), this "rip-off" brings East Germany much needed hard currency and imposes a financial burden on those who would like to visit with their relatives in East Germany with some frequency.

Prior to October 1980 the required exchange was 13 DM (traveling from West Germany to East Germany) and 6.50 DM (traveling from West Berlin to East Berlin), with an exemption from the requirement for children and pensioners. This daily currency exchange requirement was increased on October 13, 1980, to 25 DM for all visitors regardless of age or origin of travel. This increase reduced travel to the GDR and East Berlin from eight million visitors in 1979 to five mil-

lion visitors in 1981, a 40 percent reduction. Chancellor Schmidt tried to obtain an easing of this blackmail in his summit meeting with East Germany's Chairman Honecker in December 1981, but has received no positive response.

The understandable desire for West Germans to maintain their ties to relatives living in East Germany is a fact which the Soviets have cynically attempted to exploit in the past and will probably use again. It is clear to me that this question of access rights is a factor which will inevitably be used by the Soviets in their attempts to forestall the nuclear modernization plans of West Germany.

During the visit I spent several hours in East Berlin in discussions with our Embassy personnel and in driving through the city. East Germany differs from the other Iron Curtain countries in several main respects. East Germans alone amongst the Warsaw Pact peoples are not Slavic/Asian in origin and culture. As a result, there is a tendency on their part to look down on their Communist neighbors.

The East German church, largely Lutheran, is very strong, and probably better attended than the churches in West Germany. After many years of strife between the churches and the East German government, the government in 1978 conceded that the churches could not be suppressed. A great deal of freedom followed, including the ability of the churches to publish uncensored material and their right to offer viewpoints which differ from the views of the East German government.

Television has an enormous impact on most East Germans, who receive West German news and programs and who accept their credibility since they represent the same commercial television seen by West Germans. Whereas Voice of America type broadcasts are seen as propaganda by East Germans, West German TV is regarded as factual.

East Germany is also affected by the very large undergraduate university system in West Berlin, which has high attendance since West German youths can avoid conscription in that city. Such a phenomenon and the resultant opportunity for the students to cross over into East Germany brings East Germans into frequent contact with West German youths. They envy their freedom. For their part, the first hand exposure of western youths to communism strengthens their inherent opposition to that form of government.

The ethnic national ties of East Germans to West Germany persist, and there continues to be a question of the loyalty of East German troops to the Soviets should an East-West war occur in Central Europe.

Taken in the context of all other events taking place in NATO, the military, political, and economic forces at work in East and West Germany are cause for concern on both sides of the Iron Curtain.

ECONOMIC ISSUES

THE PIPELINE DECISION

The issue most on the mind of our NATO allies during my visit was the President's June 18th decision to block the sale to the Soviet Union

of U.S. licensed equipment and technology for use in construction of the natural gas pipeline from Siberia to Western Europe. In Germany, France, and the United Kingdom every single conversation, including those intended principally to cover purely military matters, quickly turned to economic issues and particularly to the pipeline. Nothing seems to have symbolized the crisis within NATO and to have fanned the fires of disagreement and dissension as has the pipeline decision. I was frankly surprised at the vehemence of this opposition to the U.S. action. French Foreign Minister Cheysson subsequent to my visit described the pipeline dispute as a "progressive divorce" developing between the United States and Europe. Based on my discussions, that is an understatement.

The basic European concern, I believe, is that the United States today is acting with indifference and/or insensitivity to the national interests of our NATO allies. The two most obvious examples they cite are the June 18 pipeline sanctions decision itself, which is incomprehensible in their eyes, and the abruptness of this decision to expand the sanctions, which Europeans allege was made without proper consultation or warning.

Because of the importance of this issue to the NATO alliance, and because it is pivotal to subsequent U.S. trade policies with the Eastern Bloc, a good deal needs to be said about the subject, as seen from the European vantage point. As will be obvious from the comments to follow, the urgent attention of the Administration to this problem seems essential.

THE LOGIC OF THE DECISION

Both anger and confusion over the decision was evident throughout my visit, and to a certain extent the confusion is the result of divergent signals being given the Europeans by various U.S. officials. For example, U.S. officials in Brussels were contending that potential European energy dependence on the Soviets was the real reason for the decision; in Bonn, the argument was that we opposed the excessive subsidization of credits; in Paris, economic warfare with the East was proffered as the basis for the President's decision; and in London the official State Department position, that our sanctions were a reaction to the Polish situation, was given. My conclusion after all this was—if I am getting conflicting views from my own Government, what impressions do we expect our own allies to have?

How do these comments sound to our allies? We continue to assert on an official basis that the reason for the U.S. action was the continued oppression in Poland. Indeed, the direction provided to our embassies from Washington not only clearly cites Poland as the reason for the sanctions, but it indicates it is the reason to the exclusion of all others. The same position was taken by Secretary of State Shultz in his confirmation hearings before the Senate Foreign Relations Committee. But that reason is categorically not accepted by our allies as the reason. They don't believe that explanation and, frankly, neither do a number of U.S. officials in Europe.

When the Europeans ask whether or not we would relax the sanctions if tensions were eased in Poland, many U.S. off-the-record comments suggest that the United States would be in an awkward posi-

tion if the Poles (or Soviets) so responded, because the United States would still be adamantly opposed to the pipeline.

Consider the European thinking. They note that although the original December 1981 sanctions coincided in timing with the Polish martial law decision, thus tying the decision directly to the Polish situation, further tightening of the sanctions in June 1982, while allegedly related to Poland, bore no relationship in timing to any specific event(s) in Poland. Probably of greater significance is the question in their minds of why sanctions on the pipeline are tied to Poland at all? We seem to be indicating that if Lech Walesa and the other Solidarity Union leaders were released and permitted to resume their pre-martial law activities, we would lift the sanctions and permit the pipeline project to go on with Western support. Is that really what the administration wants or expects?

Our NATO allies are convinced that such a reversal of Polish/Soviet policy is impossible, given the current international situation. But even if the Polish Government surprised the world and forced us to reverse our position and withdraw the sanctions, couldn't the Polish authorities later put Lech Walesa and the others back in confinement? Would it then be our policy to reimpose the sanctions on the pipeline? When one looks at this sort of scenario, the connection to the Polish situation becomes illogical in European eyes. What is missing is the recognition, according to our allies, that the United States requires a policy that is not event oriented, one that has a logical basis which can be articulated to our friends and understood by our foes. And so, European thoughts turn to speculation of what really might be behind the U.S. action.

The argument by some of our people that the pipeline would increase NATO dependence on the Soviets and subject NATO to pressure (or blackmail) also falls on deaf ears in Europe. It is simply not believable in European eyes. They point out that the Soviet gas will represent only five percent of West German energy requirements and 30 percent of its gas usage. Besides, they contend, were the gas cut off the Germans could compensate for the loss by purchasing gas from The Netherlands and perhaps from Norway.

Our NATO allies also point out that some time ago the United States had expressed alarm about growing European dependence on Mideast oil. The pipeline therefore is a logical European response to our concerns and the need for diversification of energy sources. They also point out that at Ottawa the United States had promised to find energy alternatives for European countries, a commitment that has never produced any concrete results. What, therefore, did the United States expect the Europeans to do?

Another U.S. official in Europe used as a rationale the fact that the Soviet Union is in the process of a 50 percent-plus expansion of its natural gas production, and that the amount of gas destined for West Germany was less than 15 percent of the new capacity. The remainder will be consumed internally by Soviet industries that will convert from oil to gas. Such oil savings will permit the Soviets to export oil for hard Western currency. In the view of that U.S. official, therefore, any stopping or slowing of the Soviet gas expansion program, including the pipeline, was beneficial to U.S./NATO interests.

A number of opinions were voiced that the reason for the sanctions ought to lay in U.S. concern over the unusually favorable credit terms offered the Soviets. West German Banks are offering $1.6 billion in credits at 7.8 percent interest, with—and very importantly—the guarantee by the West German government through the Hermes Export Credit Guarantee Corporation, the insurer of the creditors, for 85 percent of the financing. While some people contended that this is standard German practice, they concurred that without the Government guarantee the banks would not have extended the credits.

Examples of the more direct subsidization of credits are found in the other European participants in the pipeline deal. For example, in February 1980 (shortly after the Soviet invasion of Afghanistan) the French entered into an Export Credit Protocol with the Soviets. Pursuant to that agreement, in September 1981 credits were extended to the Soviets for the pipeline deal at a 7.8 percent interest rate, using a blending of commercial funds and very low interest money from the Bank of France. Similar direct credit subsidization has occurred in both Italy and Great Britain. It is interesting that of all the potential reasons given for the sanctions, this direct and indirect subsidization of credits was the most understandable one in European eyes. One must quickly add that while this is the most understandable reason, much of Europe is in total disagreement with the premise behind it.

In discussing the credit issue one runs head-on into differences of opinion over the fundamental question of how to deal with the Soviet Union. Our NATO allies are horrified by U.S. discussion of waging economic warfare with the Soviets, and believe it is a potentially disastrous course of action. They have an unshakeable belief that contact and trade with the Soviets is healthy, and will serve our mutual long-term interests. It follows in their minds, therefore, that if trade is good, the extension of credit is good on whatever financial terms seem prudent and appropriate to the nation making the sale. If one buys that argument, then one has to accept the argument that the subsidized European credits are acceptable. If, on the other hand, one follows the general United States approach (1) that communism is an unworkable economic system and Western economies should not compensate for the unworkability of the communist system; and (2) that the Soviets have used détente and the favorable trade concessions that followed to subsidize their military buildup, one has to be opposed to the unusually favorable credit terms being offered by the Europeans on the pipeline deal. The traditional U.S. posture has been that trade with the Soviets is acceptable if conducted on normal commercial terms, but is unacceptable if accomplished on "sweetheart" terms. Therefore, using that argument, we can rationalize our sale of grain to the Soviets on a cash basis as being acceptable.

Our NATO allies, however, say that the larger issue is trade, and in their eyes it follows that grain sales and pipeline equipment sales are one-and-the-same. Therefore, in their view, if grain sales are all right, pipeline equipment sales are all right. And within the broad policy that trade with the Soviets is acceptable, the country of origin of the sales should determine what the terms of the sale are without outside comment, criticism, or interference. They argue that such interference shows insensitivity to national sovereignty. Thus, some of my

BEST AVAILABLE COPY

discussions brought forth the opinion that the United States was hypocritical in its approach to the grain sales, and was caving in to U.S. domestic politics while denying Western Europeans the right to respond to their own domestic politics.

There could not be a sharper division among the allies than in our fundamental approaches to East-West trade.

THE ABRUPTNESS OF THE DECISION

During the trip I heard repeated complaints about the United States taking precipitate action without proper consultation of our allies. Such unilateral action, involving extraterritorial implications and breach of contract, shows extraordinary insensitivity and is absolutely unacceptable, in the words of our allies. They then expand these comments to include the charge that the United States does not have a coherent and consistent economic policy toward the Soviet Union. All of these challenges are phrased in near acrimonious terms.

While it is clear to me that at the highest levels of European government no one should have been surprised by the President's decision, Europeans profess to be astonished by the decision. Some of our embassy personnel also were apparently surprised, and point out that their ability to function effectively hinges on their being in a position to warn and attempt to pre-sell our allies on major decisions. To the extent that our embassies were not informed in advance and thus not in a position to give such warning, the conclusion of our allies that the United States made a hasty and ill-considered decision is somewhat understandable. Also, the lack of consistency in our European embassies in explaining the basis for the President's decision undoubtedly contributed to our allies' conclusion that this decision and its implications were not well thought through.

There is also confusion in Europe about events in the several months preceding the June 1982 decision by President Reagan. In March of this year all those concerned with this issue seemed to have understood that the President was considering revocation of the December 1981 pipeline sanctions, but that any action would have to await the outcome of the discussions to be conducted by Under Secretary of State James L. Buckley. The purpose of his mission to NATO was not to address the pipeline issue, per se, but to secure from the Europeans agreement that future trade with the Soviets would not involve subsidized credits of the kind given on the pipeline deal. However, the implication certainly was conveyed to our allies that the President would relax his sanctions on the pipeline if agreement was reached on credits. Such an implication at that time certainly fueled later European suspicions (see previous paragraphs) that the formal reason now being given for pipeline sanctions—a response to repression in Poland—is clearly not the reason for expanded pipeline sanctions.

Our NATO allies concur that the subject of credits was discussed during the Buckley meetings, but the Europeans now act as if they came away from those meetings with the belief that even though no agreement was reached—they indicate they basically rejected the U.S. proposals—the United States would not broaden the sanctions on the pipeline. Why they should have reached that conclusion is not clear to me, but such a conclusion is consistent with their later expres-

sions of shock and outrage when the decision was announced. The fact that our embassies also appeared surprised by the June 18 decision lends credence to that conclusion.

Our allies appreciate that the post-Versaille "business-as-usual" statements by French President Mitterand and West German Chancellor Schmidt—to the effect that the Versailles agreement on exercising "commercial prudence" in granting credits was meaningless—placed President Reagan in an awkward, if not impossible, position. They recognize that had the President not taken some action he would have appeared to have backed down from his earlier commitment that, failing a lessening of oppression in Poland, some additional action would be taken. However, Europeans still don't believe the broadened sanctions should have been imposed. In European eyes they represent unilateral breaches of contracts (retroactive imposition of sanctions on signed contracts) at a minimum. That is unacceptable to many Europeans who profess that international trade is impossible unless all parties hold sacred their contracts, whatever the subsequent turn of political events. Europeans note that the sanctions imposed against Argentina as a result of the Falklands crisis were prospectively, and not retrospectively, imposed. The extension of U.S. sanctions to European firms holding licenses on U.S. technology and equipment was universally condemned during my visit and therefore will likely be tested in court.

CONCLUSIONS ON THE PIPELINE

Two actions seem required as a result of the current pipeline dilemma: (1) to reach some compromise with our European allies which would permit the lifting of the ban in return for some meaningful trade concessions on their part; and (2) the establishment of a long-term policy with respect to East-West trade relations.

With regard to the pipeline issue, some Europeans suggested that the pipeline decision was simply a bad mistake and that it should be reversed on its own merits. I responded that there was no way that the United States would simply back off the decision and that some substantive European recognition of U.S. concerns would be required. When asked about a possible compromise, I defined U.S. interests as being that the single most important principle to be applied to East-West trade is that such trade should not be the equivalent of foreign aid—help of the type given to a developing third-world country. Any compromise should include a long-term agreement eliminating subsidies of financial credits on all future sales and insuring that the CoCom agreements on transfer of high technology of possible military application are strictly enforced.

If we provide credits to the Soviets at rates more favorable than we extend to credit-worthy, friendly trading partners, we subsidize the economic growth of the Soviet Union and thereby enable it to continue to divert its technology and resources to its massive military build-up. The bottom line must be putting into practice no less than was agreed to in principle at Versailles, that a rule of "commercial prudence" will be applied. If we and our allies want to trade with the East on the basis of cash-on-the-barrelhead, or credits at current unsubsidized commercial rates, that is a legitimate application of the

free-trade philosophy. But a deal like the pipeline which is based on heavily subsidized credits flies in the face of commonsense and the fundamental purpose of the NATO alliance. Of course, the transfer of high technology to the East makes even less sense and must be stopped at all costs.

The need for NATO to reach agreement on an overall approach to East-West trade relations seems fundamental. NATO cannot continue to exist with some of the partners believing that we should wage economic warfare with the Soviets while others believe we should extend them very attractive credit concessions. During one of the discussions on my trip the suggestion was made that very senior individuals representing each of the NATO countries should convene in the near term to come to grips with the issue of what trade policy makes sense in the coming years. This makes very good sense to me after having seen first-hand the European reaction to current U.S. policy. The resultant recommendations—a 1980's version of the 1967 Harmel Report—should be reviewed by all concerned and when a trade policy is finally evolved, NATO should speak and act with a single voice.

STEEL AND AGRICULTURE

The issue of subsidized trade arises not only in the case of the pipeline, but also in highly sensitive U.S.-European trade in steel and agriculture. The world-wide economic recession and the overcapacity in both these industries has tempted each involved nation to become more inward looking, more protectionist, and more nationalistic. "National solutions" to problems are sought rather than solutions which make sense on an international level. U.S. farmers and steelmakers have not only charged our European allies with yielding to this temptation and subsidizing steel and agricultural products, they have, at least in the case of steel, obtained Commerce Department action to impose countervailing duties on steel exports to the United States proportionate to the determined amount of subsidy.

European steelmakers in those countries affected by the duties do not want any U.S. interference and argue vehemently on the definition of what is a subsidy. The British Steel Corporation presents a unique circumstance in that it readily admits that the government is covering its losses over the several year period while they get rid of their excess capacity (over 90,000 employees have already been released), while striving for the goal of becoming an efficient, unsubsidized, profitmaking company. But few in Europe want to listen to the facts on unemployment in the U.S. steel industry and its current production at less than 50 percent of capacity.

Discussions with European Economic Community (EEC) officials indicated some optimism that a voluntary restraint agreement may be worked out based on some formula related to historic shares of the market. Adherence to voluntary agreements, however, and the reaching of more definitive, long-term agreements seem to be overly optimistic hopes given the economic difficulties in the steel industry on both sides of the Atlantic.

In terms of its impact on the NATO alliance, the dispute over dumping of subsidized steel is more disturbing in what it symbolizes with regard to protectionist attitudes. The tendency to look inward

and protect one's own parochial interests is greatly heightened by the kind of economic difficulties existing today. Although I spent very little time discussing agricultural trade, the discussions I did have indicated that it is an even worse example of individual national policies coming to the fore. The policy in certain countries is to produce all you can without regard to the market, and rely on subsidies to insure sale of the products. If such attitudes persist and spread to other industries, the alliance could well be in for open trade warfare of the kind that preceded and helped precipitate World War II. Sadly, I see the protectionist lobbies also at work in the United States.

CONCLUSIONS

The failing economies of the NATO alliance are propelling us on a collision course with one another and the world is heading for a new wave of neo-protectionism which, if carried to the extreme, can lead to economic disintegration of the Western countries.

Neo-protectionism does not always take the obvious form of higher tariffs, but is often working through the more subtle ploys of dumping, subsidization, and the erecting of difficult market regulations for foreign trade.

The possibility of a trade war is being raised by the increasing application of such measures by many nations, ourselves included. The deepening of the 1981–1982 recession has led to an increase in domestic unemployment heavily concentrated in certain industries, particularly steel and autos. As a result, some commentators have voiced fears that pressures toward protectionism could lead to a "replay of the 1930s," when international trade nearly ground to a complete halt because of "beggar-thy-neighbor" policies. Domestic economic problems are today, as in the 1930s, being atrributed in some quarters to the actions of foreign powers, rather than to our own policies and economic performance. We may be witnessing events of the kind which led to passage of the Smoot-Hawley Tariff Act of 1930, a measure which helped stifle international trade and deepened the Great Depression, thereby setting the stage for the economic and military upheavals which followed.

The distressing point is that one doesn't need to be reminded that World War I and II were triggered as much by internaticnal economic distress as by expansionist policies. In this day of the abstract potential of nuclear holocaust, it is easy to emphasize military rather than economic concerns. Our greatest challenge, however, is to preserve a viable basis for equitable international trading, before protectionism leads to world-wide economic ruin and greatly increased international tensions.

Unfortunately, the gravest problem confronting the free world today is that our allies and many people in this country thus far have failed to realize that such a problem exists. As a matter of fact, a leading French parliamentarian facetiously remarked to me over lunch that what Europe really needs is another Marshall Plan. Thus, the conventional thinking in Europe implies that the economically strong United States, impervious to the effects of its own recession, will once again "bail-out" our European allies.

BEST AVAILABLE COPY

Such thinking is incomprehensible, and the sooner our allies realize that unsubsidized free trade and accesss to markets are a two-way street, the better off we'll all be. Where one of the major European complaints is that we are insensitive to their problems, it is equally apparent that they are oblivious to ours.

When one reflects on the potential for large-scale hostilities and the possible decline of the economic vitality of Western civilization, the debate usually focuses on relative military strength and the concept of deterrence. Though providing a viable deterrence to the Soviet threat is a challenge which cannot go unmet, I believe that the potential for disaster in the eighties and beyond may arise more from economic and trade failure, than from military imbalances or military adventurism.

○